

ECONOMIC  
DEVELOPMENT

## ECONOMIC DEVELOPMENT

There were some signs of economic progress in Iraq this year.

Inflation improved, dropping from 65% at the end of 2006 to approximately 37% by the end of February 2007,<sup>407</sup> but it subsequently increased, reaching 46% by the end of June.<sup>408</sup> The primary cause of the spike was shortage of refined fuel products.<sup>409</sup> Overall, inflation remains lower than at the end of last year but is still above IMF targets.

Iraq's Central Office for Statistics and Information Technology measured unemployment at 18% and underemployment at 38% in its November 2006 annual employment survey.<sup>410</sup> However, current estimates of Iraq's unemployment rate range from 25–40%.<sup>411</sup>

Dormant state-owned enterprises (SOEs) exacerbate the unemployment situation. As reported by the Deputy Undersecretary of Defense for Business Transformation, an estimated 500,000 employees of SOEs are not included in the unemployment statistics and continue to receive only about 40% of their pay.<sup>412</sup>

The security crisis also constrains private sector development. According to the IMF, “if the level of violence can be reduced, the government investment program, including in the

oil sector, could be implemented and private sector activity could begin to recover.”<sup>413</sup>

### U.S. Task Force To Improve Business and Stability Operations

Economic activity in Iraq was prompted this quarter by a series of factory restarts by the U.S.-funded Task Force to Improve Business and Stability Operations (TF-BSO).

As of July 5, 2007, TF-BSO had conducted assessments of more than 64 major industrial operations<sup>414</sup> and selected 19 factories for restart in 2007.<sup>415</sup> The President's revised FY 2007 supplemental request of March 9, 2007, stated that TF-BSO will “help re-start over 140 Iraq factories during the next 6 to 18 months, employing up to 150,000 people.”<sup>416</sup> As of July 5, 2007, six factories have restarted production operations.<sup>417</sup>

TF-BSO reported that less than \$200 million is required to restart most of these factories; however, it has only \$50 million in appropriated funds.<sup>418</sup> To close the gap in funding, TF-BSO has attempted to negotiate with the Ministry of Finance and the Ministry of Industry and Minerals to establish a low-interest-rate loan program through state-owned banks.<sup>419</sup>



## IMF Stand-By Arrangement (SBA)

The IMF's SBA stipulates specific measures that Iraq must implement to resolve problems with balance of payment, subsidies, and other economic issues.<sup>420</sup> According to the President's *Initial Benchmark Assessment*, Iraq is on track to meet the SBA's requirements; however, to benefit from a planned follow-on IMF program, Iraq must continue to increase its fuel prices.<sup>421</sup>

An IMF progress report on the SBA in March 2007 found that Iraq has made advances in implementing many required economic and structural reforms, including:<sup>422</sup>

- launching a new national payments system
- agreeing on a comprehensive bank reform and restructuring program to promote financial soundness and provide essential services to the population
- establishing budgetary targets, especially on capital investment

- implementing monetary policies aimed at decreasing inflation

As required by the SBA, the Central Bank of Iraq (CBI) has tightened monetary policy and adopted a policy of gradual appreciation of the dinar through incremental increases to relieve inflationary pressures. Since November 2006, the dinar has appreciated 17%.<sup>423</sup> The current exchange rate is 1,249 dinars to the dollar, as of July 12, 2007. A year ago, the rate was 1,472 dinars to the dollar.<sup>424</sup> Figure 2.76 shows the historical trend for the exchange rate.

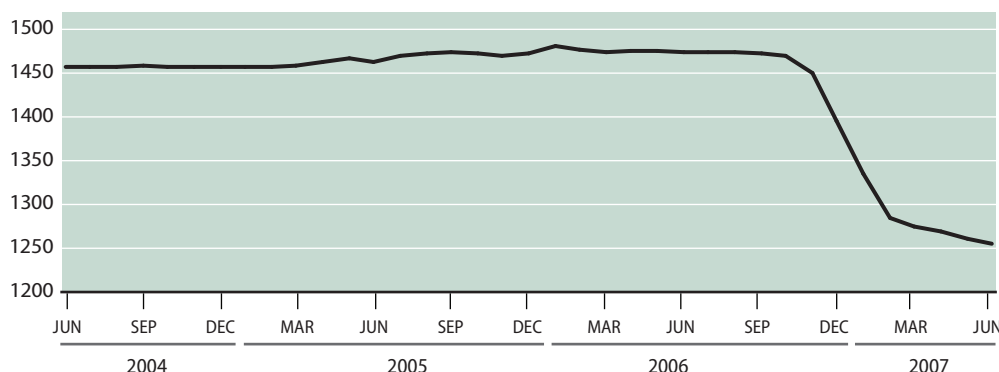
During the past quarter, Iraqi authorities have taken steps to comply with the requirements of the bank restructuring program, which they agreed to with the IMF last March. In particular, the Iraqis have focused on restructuring the two largest state-owned banks—Rafidain and Rasheed—under the SBA program as follows:<sup>425</sup>

Figure 2.76

### CURRENCY EXCHANGE RATE

Currency (Auction Selling Price Dinar/\$1 USD)

Source: Central Bank of Iraq





- In March 2007, the economic committee of the Council of Ministers approved memoranda of understanding (MOUs) for operational restructuring of both state-owned banks and a financial institution restructuring of the Rasheed bank.
- The CBI set up a bank Restructuring Oversight Committee.
- An international auditor was selected in early June to conduct an operational and financial audit of both banks and will be appointed shortly.

These measures are important elements of the more comprehensive bank restructuring program called for by the committee's MOUs.

The IMF noted that progress was sufficient to justify extending the SBA to September

2007.<sup>426</sup> The next SBA staff review is expected to take place in August, when the IMF will review progress through June 2007.<sup>427</sup>

## U.S. Support

Approximately 71% of U.S. allocations to this sector are from IRRF 2. Figure 2.77 shows the sources of U.S. funds for projects in the economic development sector.

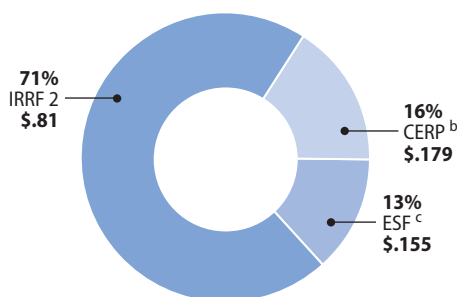
All of the IRRF allocated to economic development has been obligated, and approximately 97.5%<sup>428</sup> has been expended. As IRRF comes to an end, U.S.-funded efforts to promote economic development will continue through ESF and CERP. Approximately 16% of funds in the economic development sector are from CERP, and 13% are from ESF. Figure 2.78 shows the status of U.S. funds that have been obligated in this sector.

Figure 2.77

### ALLOCATIONS TO ECONOMIC DEVELOPMENT

\$ Billions, % of \$1.14 Billion

Sources: DoS, *Iraq Weekly Status* (6/27/2007); MNC-I, Response to SIGIR (7/7/2007); ITAO,<sup>a</sup> *Weekly Status Report* (6/26/2007)



Note: Numbers are affected by rounding.

a. By Executive Order, on May 8, 2007, the President created ITAO as the successor organization to the IRMO.

b. Allocation detail at the sector and subsector level for CERP is currently unavailable; therefore, the percentages for CERP are calculated using FY 2006 and FY 2007 dollars obligated.

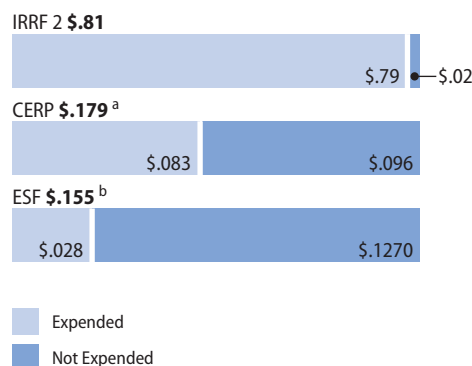
c. FY 2006 Supplemental Funds (P.L. 109-234).

Figure 2.78

### OBLIGATIONS FOR ECONOMIC DEVELOPMENT

\$ Billions, \$1.14 Billion Total

Sources: DoS, *Iraq Weekly Status* (6/27/2007); MNC-I, Response to SIGIR (7/7/2007); USAID, *Activities Report* (7/12/2007)



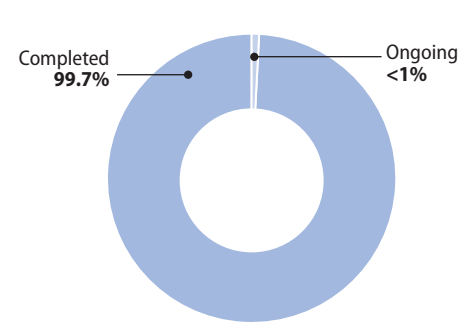
Note: Numbers are affected by rounding.

a. FY 2006 and FY 2007.

b. FY 2006 Supplemental Funds (P.L. 109-234).



Figure 2.79  
**STATUS OF IRRF 2 PROJECTS - ECONOMIC DEVELOPMENT**  
TOTAL NUMBER OF PROJECTS: 379  
Source: USAID, *Activities Report* (7/12/2007)



This quarter, the FY 2007 supplemental appropriations bill provided \$57.4 million of ESF funds to be made available to nongovernmental organizations (NGOs) in Iraq for economic and societal development programs.<sup>429</sup> Additionally, the supplemental appropriation provided \$50 million to be made available to the TF-BSO through the Iraq Freedom Fund.<sup>430</sup>

**IRRF**

IRRF-funded initiatives have been key elements in the promotion of Iraq’s economic development. IRRF funds have spanned multiple areas of economic growth promotion—from expanding the microfinance industry to providing advice on the implementation of financial systems. ESF funds are continuing many IRRF projects. Figure 2.79 shows the status of IRRF-funded projects in this sector.

**Agriculture Industry Development**

USAID has been responsible for almost all IRRF funding for the agriculture subsector

Project Type	Not Started	Ongoing	Completed	Total
Agriculture		1	374	375
Vocational Training			3	3
Market-Based Reforms			1	1
Total		1	378	379

through the \$100 million **Agriculture Reconstruction and Development Program for Iraq (ARDI)**, which focused on production, infrastructure, and capacity-building projects. The program officially closed in December 2006.

The ESF-funded **Inma Agribusiness Program** is expected to continue USAID’s efforts in these areas, under a contract with a ceiling value of \$343 million.<sup>431</sup> To date, \$37.5 million has been allocated, and the contract includes two option years.<sup>432</sup>

USDA and Texas A&M University (TAMU) agreed to a work plan for the **Iraq Agriculture Extension Revitalization Project**, and the project money will be transferred to TAMU for implementation.<sup>433</sup> The University Consortium, comprising five U.S. universities (led by Texas A&M), and six Iraqi universities, will conduct a series of two-week trainings for extension specialists on farming, poultry production, crop production, and other topics.<sup>434</sup>



### Economic Governance

Despite security issues, the USAID **Economic Governance (EG) II Project** team continues to supply technical assistance to the GOI to facilitate fiscal and monetary management through a contract valued at approximately \$225 million. As of July 9, 2007, approximately \$161.7 million of these funds had been obligated, and \$131.3 million had been expended.<sup>435</sup>

Implementation of the **Financial Management Information System (FMIS)** has been suspended indefinitely for security reasons.<sup>436</sup> Before the suspension, several technological updates were made to the FMIS. New software was configured and installed on the system to accommodate revised accounting rules, and the Government Financial Statistics-compliant Chart of Accounts was entered into the system.<sup>437</sup> To date, USAID reported that it obligated approximately \$18 million (including security costs) for the FMIS.<sup>438</sup> The figure does not include what ITAO has spent on FMIS-related modules. ESF funds are intended to complete the rollout of FMIS.<sup>439</sup>

SIGIR currently is conducting an audit to review the effectiveness of the FMIS contract.

As of April 2007, with the assistance of the U.S. Treasury, the connection of the CBI to the **Real Time Gross Settlement (RTGS)** and **Automated Clearing House (ACH)** systems was completed.<sup>440</sup> Additionally, four more private banks were accepted as users of the RTGS and ACH systems, bringing the total population of users to 11 banks and the CBI.<sup>441</sup>

U.S. efforts also helped the GOI develop a work plan and meet the deadline imposed

by the IMF Safeguards Assessment for the implementation of the **International Financial Reporting Standards (IFRS)** as the basis for financial reporting. The implementation of the IFRS is on schedule.<sup>442</sup>

### Private-sector Development Program (Izdihar)

The existing **Izdihar Private Sector Development** contract ends on September 30, 2007.<sup>443</sup> Izdihar's activities currently span multiple areas, including investment promotion, trade policy and market access, business management services, capital market development, small and medium enterprise development, and sustainable microfinance development.

### Trade Policy and Market Access

Progress on Iraq's accession into the World Trade Organization (WTO) occurred this quarter. On May 25, the Iraqi delegation to the WTO Working Party held bilateral meetings with U.S., Arab, and European delegations. As a follow-up discussion to this meeting, advisors from the Izdihar program met with the Minister of Trade, who attended the WTO meeting, to discuss several key priorities for Iraq's accession. One of the key priorities is to complete and submit the Legislative Action Plan to the WTO Secretariat.<sup>444</sup> These steps, supported by USAID, continue to drive economic reform in the key areas of trade, customs, and intellectual property rights as part of the WTO accession process.<sup>445</sup>



## Small and Medium Enterprise Development

As of July 2007, the Iraq Company for Bank Guarantees (ICBG) had approved 18 loan guarantees with a total value of \$344,279.<sup>446</sup> In November 2006, ICBG started its operations to improve access to credit and to develop profitable portfolios for qualified small and medium-sized enterprises. The program also aims to strengthen the cash-flow-based lending practices of qualified participating banks. Bolstered by a \$5 million grant from USAID through Izdihar, 11 private Iraqi banks subscribed \$3.7 million in initial equity as of April 1, 2007.<sup>447</sup>

## Sustainable Microfinance Development

Since U.S.-funded microfinance efforts began in August 2003, a total of more than \$100 million<sup>448</sup> in loans has been issued in 16 of 18 provinces.<sup>449</sup> There are \$23 million in outstanding loans to more than 18,000 clients, and

the repayment rate is more than 98%.<sup>450</sup> Izdihar began microfinance efforts in November 2006.<sup>451</sup>

## ESF

Two ESF FY 2006 Supplemental programs are categorized in the economic development sector. Figure 2.80 depicts the status of ESF-funded projects in this sector. Some ESF projects are a continuation of the efforts started by IRRF-funded activities.

## Community Stabilization Program in Strategic Cities

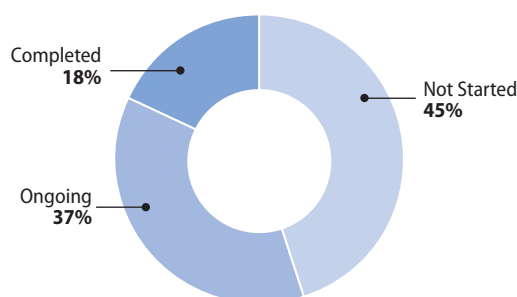
The **Community Stabilization Program (CSP)** was scheduled to end on September 30, 2008, but it has been extended to September 30, 2009, with the FY 2007 obligation.<sup>452</sup> The program is in the initial phase for assessment of additional cities.<sup>453</sup>

Figure 2.80

### STATUS OF ESF\* PROJECTS - ECONOMIC DEVELOPMENT

TOTAL NUMBER OF PROJECTS: 132

Source: USAID, *Activities Report* (7/12/2007)



Project Type	Not Started	Ongoing	Completed	Total
Community Stabilization Program	59	49	23	131
Policy and Regulatory Reforms		1		1
<b>Total</b>	<b>59</b>	<b>50</b>	<b>23</b>	<b>132</b>

\* Funded by the ESF FY 2006 Supplemental.



As of April 2007, DoS reports that CSP has:<sup>454</sup>

- expanded to Kirkuk, Mosul/Telafar, and Falluja/Anbar
- planned expansion to Basrah
- conducted security assessments in Kirkuk, Mosul, and Falluja

USAID has obligated, via a cooperative agreement, all of the \$135 million of the ESF allocated for the CSP. The CSP pursues economic development incentives and provides employment support to discourage young Iraqis from participating in violent conflict. The program comprises these major components:<sup>455</sup>

- public works and small infrastructure projects
- vocational training and apprenticeship programs

- business development programs for micro-small-medium enterprises
- youth activities

As of June 25, 2007, USAID's average daily Iraqi employment total was 63,377.<sup>456</sup> The total increased to 68,183 as of July 3, 2007.<sup>457</sup>

Table 2.15 lists the average number of daily employees per work-week for the week prior to July 3, 2007, for several U.S.-funded employment programs.

Table 2.16 shows the average daily number of people employed by the CSP in several Iraqi cities. Additionally, USAID reports that approximately 8,000 people, of which 532 people are employed in infrastructure projects, have benefited from CSP in the Ninewa Province.<sup>458</sup>

**AVERAGE NUMBER OF PEOPLE EMPLOYED DAILY BY EMPLOYMENT PROGRAM**

EMPLOYMENT PROGRAM	IRAQIS EMPLOYED
USAID	68,183
GRD (includes MILCON/OMA)	18,758
CERP	4,320
MNSTC-I	11,788
IRRF Non-construction	8,855
<b>Totals</b>	<b>111,904</b>

Source: ITAO, *Weekly Status Report*, July 3, 2007, p. 17.  
Note: For work-week prior to July 3, 2007.

TABLE 2.15



AVERAGE NUMBER OF PEOPLE EMPLOYED DAILY BY THE CSP

	BAGHDAD (JUNE 24 – 30)	ANBAR (JUNE 24 – 30)	MOSUL (JUNE 10 – 16)	KIRKUK (JUNE 10 – 16)
Short-term Employment (< 3 months)	32,210	10,172	6,711	1,920
Long-term Employment (> 3 months)	11,216	99	296	801

Sources: USAID, responses to SIGIR, June 21, 2007 and July 9, 2007.

Note: Not all cities in which the CSP has operations are represented in the table.

TABLE 2.16

### Policy and Regulatory Reforms

U.S.-funded projects continue to assist the GOI in **Policy and Regulatory Reforms**, which include support to the CBI for improving monetary policy and macroeconomic analysis activities. The focus of these efforts, funded by \$20 million, includes assistance with bank restructuring, banking supervision, reserve requirement, Iraqi treasury bill auctions, and information technology management.<sup>459</sup> The program also assists the Ministry of Finance in developing an integrated annual budget, using the IMF classification system. This budget planning assistance will help the ministry prepare the national budget in accordance with the requirements of the SBA.<sup>460</sup>

In their efforts to help the GOI comply with terms of the SBA and meet the requirements of the IMF Safeguards Assessment, USAID and Treasury also performed these activities:<sup>461</sup>

- working with CBI to ensure that the reconciliation of the Net International Reserves is accomplished to meet IMF Safeguard Assessment requirements

- assisting the GOI in amending the existing approved Prudential Regulations to ensure consistency and compliance with international best practices
- helping the GOI gain approval of draft Secured Transaction legislation from the Shura Council and Ministry of Finance

ESF-funded efforts are continuing many of these activities started by IRRF funds.

### Provincial Economic Growth (PEG) Program

USAID anticipates that the **Provincial Economic Growth (PEG) Program** will provide \$10 million in loan and operational capital to microfinance institutions during each of its first two years of operations.<sup>462</sup> PEG aims to increase access to finance and promote growth for selected Iraqi manufacturing and service sectors.<sup>463</sup> It has three main components:<sup>464</sup>

- developing the private sector
- strengthening Iraqi business to grow selected sectors of the economy
- expanding commercial lending to increase access to finance





The President's 2007 supplemental and 2008 budget requests sought \$45 million for PEG; \$125 million for Inma Agribusiness development; and \$75 million for Economic Governance II.<sup>465</sup> PEG follows up on USAID's previous private-sector development project (Izdihar).

### CERP

CERP FY 2006 and FY 2007 economic development projects were allocated approximately 16% of the total reconstruction funds for the economic development sector and 19% of total FY 2006 and FY 2007 CERP funds in Iraq.

CERP economic development projects

include civic cleanup activities; economic, financial, and management improvements; agriculture, irrigation, food production, and distribution projects; and civic support vehicles (see Figure 2.81).

In Baghdad, nearly \$1 million of CERP funds are used to employ Iraqis to rehabilitate **Mustansiriyah University**, including the repair of buildings, telephone systems, and sanitation services.<sup>466</sup> More than \$400,000 in CERP funding is being used to employ local Iraqis to reconstruct **Al Nasir School** in Babil.

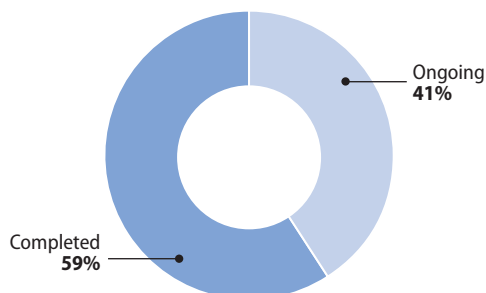
As IRRF projects in this sector finish, and IRRF funding is expended, CERP projects and funding are taking on a greater significance.

Figure 2.81

#### STATUS OF CERP FY 2006 AND FY 2007 PROJECTS - ECONOMIC DEVELOPMENT

TOTAL NUMBER OF PROJECTS 1,676

Source: MNC-I, Response to SIGIR (7/7/2007)



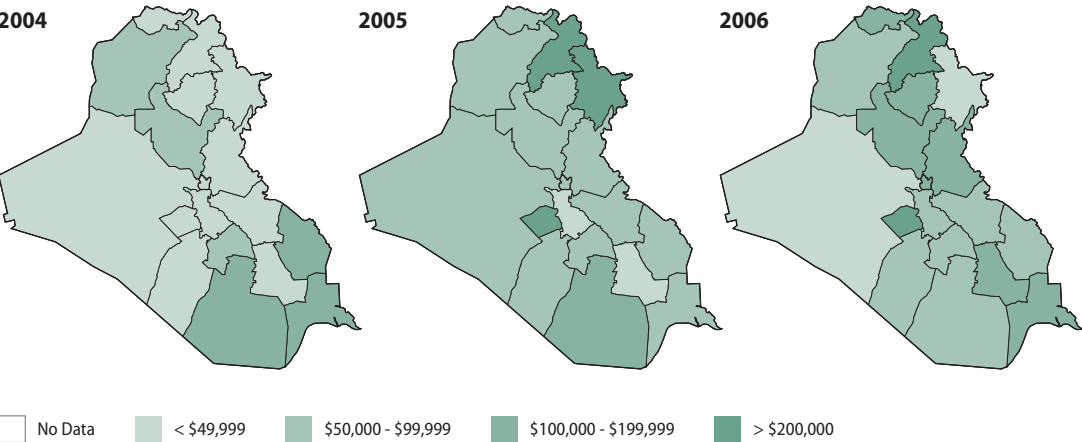
Project Type	Ongoing	Completed	Total
Civic Cleanup Activities	280	345	625
Other Humanitarian or Reconstruction Projects	221	374	595
Economic, Financial, and Management Improvements	78	70	148
Agriculture	60	87	147
Irrigation	30	61	91
Food Production and Distribution	23	30	53
Civic Support Vehicles	3	14	17
<b>Total</b>	<b>695</b>	<b>981</b>	<b>1,676</b>



MNC-I has undertaken 1,676 economic development projects with CERP FY 2006 and FY 2007 funds, completing 981 of them. In 2004, the average CERP economic development project was valued at nearly \$40,000. In 2006,

this average had increased to approximately \$120,000, and nine provinces had CERP economic development projects that averaged more than \$100,000 in value, as shown in Figure 2.82.

Figure 2.82  
**AVERAGE VALUE PER CERP ECONOMIC DEVELOPMENT PROJECT BY GOVERNORATE**  
Source: IRMS, CERP Excel Workbook (6/29/2007)



Note:  
Data is compiled using FY 2004, FY 2005, and FY 2006 CERP funds. The years indicated correspond to the actual start dates of the projects.